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DOW THEORY LETTERS

"THE MARKET AS INTERPRETED UNDER THE DOW THEORY"

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QUESTION. What would happen if a great number of people, all followers of a Dow Theory service, traded on the same advice at the same time? Would this destroy the effectiveness of the theory?

ANSWER. William P. Hamilton's famous Dow Theory editorials appeared in Barron's and the Wall Street Journal, many on the front page of the Journal. If students of the market will check the averages against the dates when these widely-read editorials were published, they will be surprised to discover that Hamilton's predictions had no effect on the market. For instance, on September 11, 1909, Hamilton stated in his cautious way: "Pessimism has never been the policy of this paper, but it published an earnest plea for conservatism when the market was at the top. Nothing has occurred since which has not emphasized the position taken." Yet after this editorial appeared, the two averages barely moved for a period of four months, then finally turned sharply down as the bear market ran its ominous course.

Hamilton wrote the following unhedged opinion on December 30, 1921. "We are in a primary bull market tending to become dull on reaction, but slowly gathering strength for a more impressive advance." Investors who made purchases here and held them grew rich as the market flowered into the 1921-29 bull market. But judging by the low volume and the listless movements that followed for months after this piece was written, few people were ready to act on the predictions of the greatest Dow Theorist of his time.

On October 25, 1929, Hamilton called the great bear market in his historic "Turn of the Tide" editorial. Thousands held their stocks in disbelief. Then a few weeks later (November 18, 1929), Hamilton warned: "It might well be thought that a decline from 381.17 to 148.69.... would represent all the deflation the most over-confident bull market could ever need. But the market is a law to itself, establishing its own precedents and accepting no others. It is saying the liquidation is not completed...At least those who look for a resumption of the old bull market may be assured that there is not a single indication in the averages that the decline is over." A short time later the public came in on a false upward move to the tune of 6-9 million shares per day. This disastrous return (on higher volume than during the bull market) eventually wiped out more fortunes than did the crash of October, 1929.

QUESTION. Why don't you mention tightening money and higher bond yields as a bearish influence on the market?

ANSWER. Under Dow Theory, tightening money, higher bond yields, the foreign situation, politics, crop reports, metal prices, and a thousand other well-known and lesser-known factors are discounted in the averages each day. The market will hand down its "bloodless verdict" long before the leading experts could possibly appraise all the factors which affect the economy and corporate profits. This "verdict," historically, will be more accurate than the opinion of any one man or group of men. Dow Theorists have learned never to argue with it.

NOTES. Prior to last week, when no letter was written, a letter had been sent each week for about six weeks. Readers should know, however, that this is not a weekly publication. There will be a minimum of forty letters per year, but their frequency will vary as the occasion warrants. Subscribers may receive two letters in a single week during a crucial period, and perhaps a letter every twelve days during a dull stretch.

As a result of my Dow Theory article in last week's Barron's, an unusually large number of requests came in for recent and older copies of these letters. I regret to say that my files are now sadly depleted. It is possible that I may have to reprint certain issues, but until

then, I offer my apologies to those readers whose requests can not be filled.

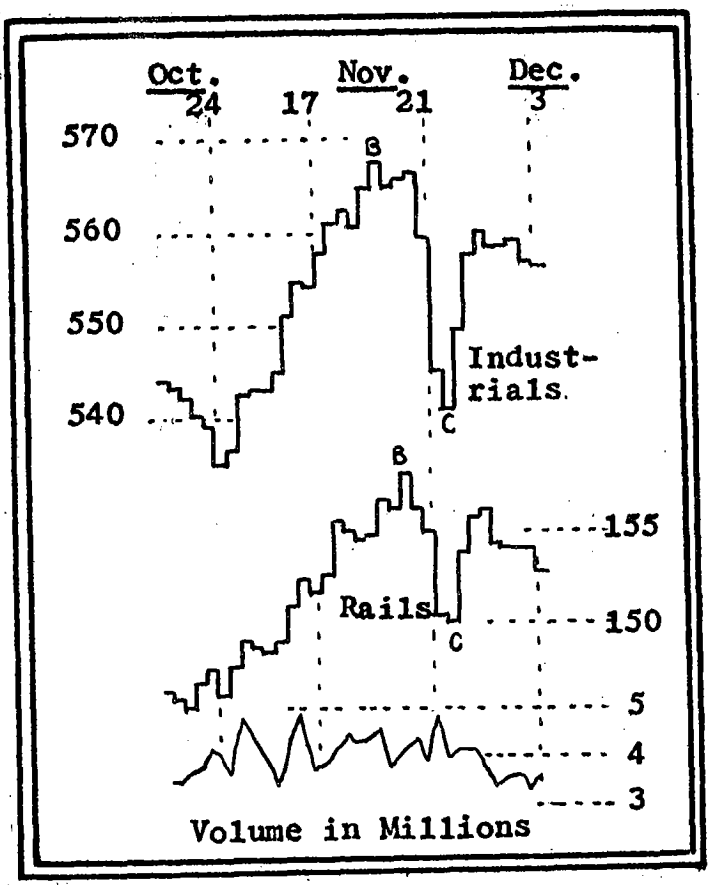
DOW THEORY. In letter #47 I pointed out that after a formation such as the panic decline of late November (B-C on chart), it is normal for the averages to advance sharply about 40-60% from the panic lows (as shorts cover), and then sag irregularly toward the lows again. A rapid advance did follow the panic, and the two averages are now in their decline area. If one or both averages now hold above the lows at C (Indust. -540.72, Rails-150.19) and volume tends to dry-up as C is approached, the picture will remain bullish, and stocks may be purchased for a rise through the highs in due time. However, if the two indicators violate their lows at C on increasing volume it will be obvious that the liquidation is not completed and still lower prices will be seen. In my opinion, the first course is the more likely one. Rails, particularly, do not seem to want to approach their lows.

This area is a sensitive one for prediction purposes. I believe that if the first possibility (outlined above) occurs, the market is saying that the business recovery is to continue and that the country will shortly enjoy an even higher level of prosperity. If the second possibility becomes reality, the market will be predicting a temporary halt or even a slight downturn in the business picture. (written Dec. 7.)

On Monday, December 8, both averages grudgingly gave ground as volume continued to register on the low side. The gradual approach to Point C goes on. Much of the hesitant action here is undoubtedly due to year-end tax-selling, short covering, and switching.

Readers who chart the averages (and I suggest this procedure to everybody) noticed that last week we had three successive days of divergence. This divergence (the two averages moving in opposite directions) is an indication of the uncertainty which grips the market. I feel the test will come within the next two weeks. It is important to remember that the longer the two averages hold above C, the better the chances of a reversal and a bullish advance over the previous highs at B. Above all, readers should note that a penetration of one average unaccompanied by the other through either the lows of C or the highs at B is a useless signal for prediction purposes and may well be deceptive. For example, if rails now plunged through their lows at C but industrials held above C, we should not sell. It would very possibly be a deceptive move. (Written Dec. 8, 9 P.M.)

	INDUSTRIALS	RAILS
Pt. B (highs)	567.44	157.91
Pt. C (lows)	540.72	150.19



The following stocks are in bullish patterns and may be purchased in the area described above. UNIVERSAL-CYCLOPS, MAGNAVOX, MOLYBDENUM, REVLON, CARPENTER STEEL, RAYTHEON, MONTEREY OIL, BELL & HOWELL, INTERNATIONAL TELEPHONE, AMERICAN TELEPHONE, POLAROID.

Low-priced speculations to buy.
SPARTON, CONTINENTAL MOTORS, ELECTRIC & MUSICAL INDUSTRIES, ADMIRAL, WELBILT.